Danaharta Managers Sdn Bhd v Huang Ee Hoe & Ors

HIGH COURT (KUALA LUMPUR) — SUIT NO D5–22–279 OF 2000
KANG HWEE GEE J
9 APRIL 2002

Contract *— Guarantee — Performance guarantee — Variation of — Whether variation discharged guarantee — Intention of parties to protect bank from non payment of loan — Borrower made cross claim against bank — Failure of bank to provide requisite letters of disclaimer to borrower — Whether discharge wholly inconsistent with purpose of providing security to bank as intended in guarantee — Whether defendants waived rights over variation by bank*

This was an appeal from the decision of the registrar in allowing the plaintiff's application for summary judgment under O 14 of the Rules of High Court 1980, wherein the defendants were jointly and severally ordered to pay a sum that arose from a performance guarantee that they had signed in favour of United Malayan Banking Bhd ('the bank') for the benefit of the borrower, Manalom Sdn Bhd. In this appeal, it was submitted that pending the disposal of the borrower's claim against the bank in another suit, summary judgment should not be entered against the defendants in this case and by reason that the bank had failed to provide the borrower with the requisite letters of disclaimer disclaiming all its right to the remaining portion of the land which it had promised to do under a debenture and a charge, there had been a variation in the terms and conditions under which the loan facilities was granted to the borrower. The variation, so it was submitted, had discharged the contract of guarantee, which the defendants gave to the plaintiff.

Held, dismissing the appeal:

(1) The guarantee that the parties had entered into was a performance bond, or properly so called, a performance guarantee, struck with the intention of protecting the bank against the non payment of the money loaned to the borrower under the facility agreement. The terms and conditions written therein must therefore be given the precise construction that the contracting parties had intended (see p 435D).

(2) Looking at the guarantee as a whole, it would be totally inconceivable under the circumstances to expect that the parties had intended the guarantee to be operative only if the bank was free from any cross-claim from the borrower as counsel for the defendants submitted. Such a construction would be wholly inconsistent with the purpose of providing the required security or protection to the bank that the parties had intended (see p 435F).

(3) The fact that the borrower may have a claim against the bank in respect of its failure to comply with its promise to release the unused portion of the land secured under the debenture and the charge as provided under cl 11 of the facility agreement would not therefore discharge the guarantors from their obligation to pay (see p 436B).

(4) The default on the part of the bank to keep to its promise (even if proved to be a breach) could not by any stretch of imagination constitute a variation of the facility agreement. By subscribing to the terms and conditions described in cl 5 of the guarantee, the defendants had waived whatever right that they may have had over any variation that the bank may have instituted over the charged property (see pp 437E–F, 438B).

[**Bahasa Malaysia summary**

Ini merupakan satu rayuan daripada keputusan pendaftar dalam membenarkan permohonan plaintif untuk penghakiman terus di bawah A 14 Kaedah-Kaedah Mahkamah Tinggi 1980, dalam mana defendan-defendan diperintah secara bersama supaya membayar sejumlah wang yang berbangkit daripada jaminan pelaksanaan yang telah ditandatangani oleh mereka memihak kepada United Malayan Banking Bhd ('bank tersebut') untuk manfaat peminjam, Manalom Sdn Bhd. Dalam rayuan ini, dihujahkan bahawa sementara menunggu penyelesaian tuntutan peminjam terhadap bank tersebut dalam satu lagi guaman, penghakiman terus tidak harus dimasukkan terhadap defendan-defendan dalam kes ini dan disebabkan bank tersebut telah gagal memberi peminjam surat kenyataan penafian yang menafikan segala haknya terhadap baki bahagian tanah yang ia telah janjikan di bawah debentur dan gadaian, telah berlakunya variasi dalam terma dan syarat-syarat di bawah mana kemudahan pinjaman telah diberikan kepada peminjam. Variasi tersebut, sebagai mana ia dihujahkan, telah membatalkan kontrak jaminan, yang telah diberikan kepada plaintif oleh defendan-defendan.

Diputuskan, menolak rayuan tersebut:

(1) Jaminan yang telah diikat oleh pihak-pihak merupakan satu bon pelaksanaan, atau gelarannya yang betul, satu jaminan pelaksanaan, yang telah disetujui dengan hasrat melindungi bank tersebut daripada ketidakbayaran wang yang dipinjam kepada peminjam di bawah perjanjian pinjaman. Terma dan syarat yang tertera dalamnya dengan itu mestilah diberikan tafsiran yang tepat sebagai mana yang diniatkan oleh pihak-pihak yang mengikat kontrak (lihat ms 435D).

(2) Dengan memandang jaminan tersebut secara keseluruhan, adalah amat sukar sama sekali di bawah keadaan begitu untuk menjangka bahawa pihak-pihak telah meniatkan jaminan tersebut beroperasi

hanya sekiranya bank tersebut bebas daripada sebarang tuntutan balas daripada peminjam sebagai mana yang dihujah oleh peguam bagi pihak defendan-defendan. Tafsiran sedemikian adalah bercanggah sepenuhnya dengan tujuan menyediakan cagaran atau perlindungan yang perlu kepada bank tersebut seperti yang dihasratkan oleh pihak-pihak (lihat ms 435F).

(3) Hakikat bahawa peminjam mungkin ada tuntutan yang sah terhadap bank tersebut berkaitan dengan kegagalannya untuk mematuhi janjinya untuk melepaskan bahagian tanah bercagar yang tidak digunakan di bawah debentur dan gadaian tersebut seperti yang diperuntukkan di bawah fasal 11 perjanjian pinjaman dengan itu tidak akan membebaskan penjamin daripada kewajipan mereka untuk membayar (lihat ms 436B).

(4) Keingkaran pada pihak bank tersebut untuk menepati janjinya (biarpun dibuktikan kemungkiran) tidak boleh walau dengan apa cara pun membentuk satu variasi perjanjian pinjaman. Dengan menandatangani terma dan syarat-syarat yang disifatkan dalam fasal 5 gerenti tersebut, adalah jelas kepada mahkamah bahawa defendan-defendan telah menepikan apa-apa hak yang mungkin boleh dituntut oleh mereka ke atas sebarang variasi yang bank tersebut mungkin telah kenakan ke atas hartanah yang dicagarkan (lihat ms 437E–F, 438B).]

Notes

For cases on performance guarantee, see 3(2) *Mallal's Digest* (4th Ed, 2000 Reissue) paras 3013–3015.

Cases referred to

Bank of Scotland v Wright [1990] BCC 663 (refd)

China Airlines Ltd v Maltran Air Corp Sdn Bhd [1996] 2 MLJ 517 (refd)

Citibank NA v Ooi Boon Leong & Ors [1981] 1 MLJ 282 (refd)

Easal (Commodities) Ltd v Oriental Credit Ltd; Banque Du Caire SA v Wells Fargo Bank NA [1985] 2 Lloyd's Rep 546 (refd)

Esso Petroleum Malaysia Inc v Kago Petroleum Sdn Bhd [1995] 1 MLJ 149 (refd)

Government of Malaysia v South East Asia Insurance Bhd [2000] 3 MLJ 625 (refd)

Malayan Insurance (M) Sdn Bhd v Asia Hotel Sdn Bhd [1987] 2 MLJ 183 (refd)

Syn Lee & Co Ltd v Bank of China [1961] MLJ 87 (refd)

Trafalgar House Construction (Regions) Ltd v General Surety & Guarantee Co Ltd [1995] 3 All ER 737 (refd)

United Merchant Finance Bhd v Hockwood Holdings Sdn Bhd & Ors [1999] 5 MLJ 85 (refd)

Legislation referred to

Contracts Act 1950 s 86
Pengurusan Danaharta Nasional Bhd Act 1998
Rules of the High Court 1980 O 14

J Kannaperan (*Shearn Delamore & Co*) for the plaintiff.
Fiona M Bodipalar (*Sri Ram & Co*) for the defendants.

Kang Hwee Gee J : This is an appeal from the decision of the registrar in allowing the plaintiff's application for summary judgment under O 14 of the Rules of the High Court 1980 ('RHC') wherein the defendants were jointly and severally ordered to pay:

(i) the sum of RM78,286,609.35 due to the plaintiff as at 30 November 1999, in respect of the term loan facility availed to one Manalom Sdn Bhd ('the borrower') with further interest continuing at Maybank Bhd's base lending rate + 2% + 1% pa, at monthly rests from 1 December 1999 to the date of full and final realization on all sums outstanding and overdue;

(ii) a sum of RM10,540,987.31 due to the plaintiff as at 30 November 1999 in respect of the standby term loan facility availed to the borrower with further interest continuing at Maybank Bhd's base lending rate + 2% + 1% pa at monthly rests from 1 December 1999 to the date of full and final realization on all sums outstanding and overdue;

(iii) the sum of RM1,000 due as costs charges and outstanding to the plaintiff;

(iv) the costs of this action on a solicitor-client basis.

The defendants liability to pay arose from a performance guarantee that they had signed in favour of United Malayan Banking Bhd for the benefit of the borrower Manalom Sdn Bhd.

Pursuant to the sale of the bank's rights, title and interest in the facilities to the plaintiff under the provisions of the Pengurusan Danaharta Nasional Bhd Act 1998 ('the Act'), by a vesting order, the plaintiff stepped into the shoes of the Bank to file this claim against the guarantors.

The facts necessary to support the application were set out in the affidavit of the plaintiff's general manager, Derrick Fernandez. They are undisputed and may be summarized as follows:

(1) By a facilities agreement dated 13 October 1994 entered into between United Malayan Banking Corp Bhd ('the seller') of the one part and the borrower of the other part ('the said facilities agreement'), the seller has at the request of the borrower agreed to make available to the borrower banking and credit facilities ('the said facilities') comprising the following:

(i) a term loan facility of RM65m and

(ii) a short term loan facility of RM8m;

(2) It is a term and condition of the said facilities agreement that: A

(i) the borrower shall promptly pay and settle the amounts advanced under the term loan facility by the 32 unequal quarterly instalments prescribed in the agreement and the amounts advanced under the short term loan facility by the 17 equal quarterly instalments as prescribed in the agreement together with the prescribed rates of interest on the term loan facility and the short term loan facility ('Prescribed Rate') at 9% pa for the first three years from the date of draw-down of the facilities, and thereafter at 2% pa above base lending rate ('BLR') all at monthly rests and payable quarterly in arrears; B

(ii) the borrower shall upon default in the payment of any monies due under the said facilities, whether principal or interest, pay additional default interest until the date of settlement of such sums; C

(iii) the borrower fails to observe or perform any of the terms and conditions of the said facilities agreement and such event of default is not remedied within 14 days from a written request to so remedy; D

(iv) the seller shall be entitled in the manner set out in the said facilities agreement to vary from time to time at its discretion the interest rates, the applicable rest periods and/or the commission and discount rates prescribed in the said facilities agreement; E

(v) the interest due on any monies under the said facilities shall be capitalized and added to the principal sum and bear interest at the applicable rate. Thenceforth, the seller's right to charge such compound interest shall subsist and continue notwithstanding service of demand and/or the relationship of lender-borrower between the parties ceasing; F

(vi) the borrower shall pay all costs, charges and expenses incurred by the seller including legal costs on a solicitor and client basis; and

(vii) the said facilities and the continued availment thereof shall be subject to the seller's right to periodically review, restructure or recall the same as the seller in its absolute discretion sees fit; G

(viii) the seller may at any time without affecting the agreement or any security document, modify or abstain from enforcing the rights that the seller may from time to time have against the borrower or any security party; H

(ix) no delay or omission on the part of seller in exercising any right, power, privilege or remedy accruing to the seller shall operate as a waiver of the same or preclude any further exercise of that right, power, privilege or remedy;

(3) Pursuant to the terms and conditions of the said facilities agreement, made available the said facilities to the borrower and the borrower has utilized the said facilities; I

(4) In breach of the terms and conditions of the facilities agreement, the borrower failed and neglected to make prompt and punctual payment of interest and principal instalments due and owing on the facilities and/or deposit the agreed RM25m with the seller on or before 30 September 1998, despite the seller having, at the borrower's request, agreed to extend time for repayment of such instalments and deposit;

(5) Pursuant to the terms and conditions of the facilities agreement, the seller vide its solicitors' letter dated 10 October 1998 provided the borrower notice that in the event the borrower failed and neglected to remedy its aforesaid breach within 14 days thereof, the seller shall proceed to declare the facilities cancelled and withdrawn;

(6) In continued breach of the terms and conditions of the facilities agreement, the borrower failed and neglected to remedy its breach and make payment of the overdue and outstanding instalments or deposit;

(7) Pursuant to the terms and conditions of the facilities agreement and the sale of the seller's rights, title and interest in the facilities to the plaintiff and the provisions of the Act, the plaintiff did by its solicitors' letter dated 1 December 1999, inform the borrower that by reason of the matters stated in paras 8 and 9, and pursuant to the terms and conditions of the said facilities agreement, the said facilities were withdrawn and cancelled and all amounts owing, unpaid and outstanding under the said facilities amounting to RM88,828,596.66 together with all continuing interest, commission, charges and expenses as particularized hereinbelow ('the outstanding sum') were due and owing to the plaintiff and demanded that the borrower within seven (7) days from receipt of such letter make payment of the said outstanding sum;

(8) In breach of the terms and conditions of the facilities agreement, the borrower has to date failed, refused and/or neglected to pay the outstanding sum as particularized in para 10 above or any part thereof;

(9) By a personal guarantee dated 13 October 1994 furnished by the defendants ('the said letter of guarantee'), the defendants have in consideration of the seller granting and lending the facilities to the borrower, jointly and severally, guaranteed to repay on demand the sums due under the facilities, together with costs, expenses and all other liabilities owing, payable and remaining unpaid by the borrower including legal costs on a solicitor-client basis;

(10) It is, inter alia, a term of the guarantee that:

(i) the said guarantee shall be a continuing security to cover any sums of money which shall for the time being, constitute the monies remaining unpaid by the borrower;

(ii) the said guarantee shall be without prejudice and not be affected, nor will the defendants be affected, released or exonerated by, inter alia:

(a) the determination, variation or increase of a credit facility to the borrower;

(b) any securities or guarantees held in respect of the monies guaranteed;

(c) any variation, exchange, renewal, release or modification of any such securities;

(d) any time, forbearance, relaxation or indulgence given or extended to the borrower and/or any other persons whether with or without consent or notice to the defendants; and

(e) any variation of any security document including the facilities agreement whether with and/or without consent or notice to the defendants;

(iii) any admission or acknowledgement in writing by the borrower or any person on behalf of the borrower of the amount of the indebtedness of the borrower shall be prima facie evidence against the defendants;

(iv) the said letter of guarantee shall be interpreted and governed in accordance with the laws of Malaysia and the defendants submits to the non-exclusive jurisdiction of the courts of Malaysia; and

(v) any demand for payment of monies due may be sent by post or delivered to the defendants' address stated therein and shall be deemed to be received at the time when the letter would in the ordinary course of post be delivered;

(vi) time for payment of the sums guaranteed shall be of the essence;

(11) Pursuant to the terms of the said facilities agreement and the said guarantee, and the sale of the seller's rights, title and interest in the facilities to the plaintiff and the provisions of the Act, the plaintiff did by its solicitors' letter dated 1 December 1999 demand payment of the outstanding sum as particularized in para 10 herein, within seven days of service thereof but the defendants have to date failed, refused and/or neglected to pay the outstanding sum or any part thereof;

(12) The defendants have however failed and neglected to pay the outstanding sum or any part thereof and continue to be indebted to the plaintiff for the said sum.

The defendants' grounds for opposing the application

The application was opposed on a number of grounds at the hearing before the registrar.

In this appeal however, counsel for the defendants had consolidated and confined her argument to two grounds, the merit of which revolves on an alleged breach by the bank of its obligation under cl 11 of the facility agreement to which I shall revert to shortly.

The effect of that breach would render the guarantee invalid, so it was argued — and pending the disposal of the borrower's claim against the bank in the other suit, summary judgment should not be entered against the defendants in this case.

A salient feature of the facility agreement

To appreciate the nature of the defendants' argument, it is now necessary to refer to cl 11.

First, it must be noted that apart from the guarantee, the borrower had also provided a debenture and charge over a piece of land held under CT 8528, Lot 2794, Mukim of Petaling, District of Kuala Lumpur ('the said land') as security for the two loans under the facility agreement.

The borrower was the registered proprietor of the said land. At the time that the said loans were granted, the said land had yet to be sub-divided. The borrower constructed a multi storey building ('the Plaza') on part of the said land ('the Plaza Land').

The debenture and the charge specifically provides that part of the said land ('the Remaining Land') was excluded from the debenture and the charge.

It therefore became necessary for the parties to provide by cl 11.3 of the facility agreement that the Bank would deliver to the borrower a letter of exclusion and disclaimer disclaiming all its rights and entitlements over the Remaining Land upon delivery of a valuation report on the Plaza valuing the same for a sum not less than RM210m.

Alleged breach by the Bank in failing to issue a letter of exclusion and disclaimer

According to the defendants, pursuant to the facility agreement, the borrower provided the Bank with the valuation report stating that the Plaza was valued at RM210m.

Pursuant to the procurement of the valuation, the Bank provided certain letters of exclusion and disclaimer to the end-financiers of purchasers of the remaining land whom the borrower had sold or intended to sell to.

However, in July 1998, when the borrower requested the Bank to provide an undertaking to return the sub-divided titles to the borrower upon issuance by the relevant authorities, the Bank refused to do so.

The defendants contended that this default on the part of the Bank resulted in the borrower being unable to proceed with the development and suffering severe loss and damage which in turn, had affected the borrower's ability to meet its financial obligations.

Consequently, the borrower, Manalom Sdn Bhd, instituted an action against the Bank vide Kuala Lumpur High Court Civil Suit No S1–22–649–98 to claim loss and damages before the Bank could bring an action to recover the loans from it. The pre-emptive move by the borrower relegated the Bank to assume a defensive position. It had to file a defence to the

borrower's claim and a counterclaim against the borrower to claim the loan.

The submission on the first ground

The borrower, it was submitted, had already commenced an action against the Bank vide Suit S1–22–649–98. In the event that the borrower Manalom Sdn Bhd succeeded against the Bank in that suit which is still pending before the court, this would mean that the borrower would not be owing the Bank any money and consequently the defendants in the instant case would not be liable as guarantors.

This was how counsel for the defendants proposed her argument in her written submission:

> 7 The defendants respectfully submit that as a result of the breach of the facilities by the Bank, the borrower did not owe the Bank any sums as at the date of the vesting order. This issue is currently before the court in the first suit. The Bank has in the first suit filed a counterclaim against the borrower claiming the amounts allegedly due under the facilities. If the court decides the first suit in favour of the borrower, this will confirm that the borrower does not owe the Bank any money. There are two consequences that will flow from such an order:
>
> 7.1 the vesting order will be null and void as the loss suffered by borrower would have been set off against any amount due under the facilities and there would be no sums to assign to the plaintiff;
>
> 7.2 the guarantors would have no liability, as the guarantors are only liable for sums due from the borrower to the Bank. If the borrower is not liable to the Bank, it follows that the guarantors have no liability.

The submission on the second ground

By reason that the Bank had failed to provide the borrower, Manalom Sdn Bhd, with the requisite letters of disclaimer disclaiming all its right to the remaining portion of the land which it had promised to do under the debenture and the charge, there had been a variation in the terms and conditions under which the loan facilities were granted to the borrower. The variation, so it was submitted, had discharged the contract of guarantee which the defendants gave to the plaintiff.

This was how counsel for the defendants proposed her argument:

> 9 The defendants further submit that the defendants had executed the guarantee on the Bank's agreement that the Bank would provide the requisite letters of disclaimer disclaiming all rights to the Remaining Land. The Bank's failure to provide the requisite disclaimer amounts to a variation which results in a discharge of the guarantee pursuant to s 86 of the Contracts Act 1950. Section 86 of the Contracts Act 1950 provides that:
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> > 'Any variance, made without the surety's consent, in the terms of the contract between the principal debtor and the creditor, discharge the surety as to transactions subsequent to the variance.'

A 10 Section 86 of the Contracts Act 1950 was applied by the Supreme Court in the case of *Kidurong Land Sdn Bhd & Anor v Lim Gaik Hua & Ors* [1990] 1 MLJ 485. In the said case, the Supreme Court held that material variations made to a contract resulted in the discharge of the guarantors who had guaranteed the performance of the said contract.

B *Finding — the first issue*

The submission calls for the determination of the exact nature of the guarantee that the defendants had given to the Bank.

To comprehend its nature, it would be necessary to look into the relevant clauses of the guarantee that the parties had committed themselves to.

C The nature of the guarantee that the defendants gave to the bank is spelt out in cl 1 of the guarantee as follows:

> Upon the happening of an event of default as defined and described under cl 14.1 of the f/agreement and the borrower shall have failed to remedy such default (which is remediable) within the time as provided in the f/agreement,
D I/we will pay to you on demand the sum under the facility, costs and expenses and other liabilities whether certain or contingent now or hereafter owing and payable and remaining unpaid to you by the borrower under and pursuant to the f/agreement ('the Indebtedness').

The term 'events of default' is defined under cl 2.1(p) of the facility agreement as:

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> the happening of the events listed in cl 14.1 which have resulted in the borrower being liable to pay the facilities or balance thereof pursuant to the provision of the aforesaid clause.

Clause 14.1 of the facility agreement provides that:

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> Upon the occurrence of any of the following events and unless the same shall not have been remedied by the borrower within fourteen (14) days from a written request to this effect by the Bank to the borrower and the Bank may at any time thereafter by written notice to the borrower declare the facilities to be cancelled and any outstanding balance thereof and interest thereon all other monies payable by the borrower under the terms of this agreement and
G the security documents to be then forthwith due and payable whereupon the same shall become so payable.

Some 17 'events of default' are listed in cl 14.1 of the facility agreement. But the event of default that the Bank was relying on is cl 14.1(a) which reads as follows:

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> the borrower or any security party defaults in the payment to the Bank of the principal interest commission or other monies payable by the borrower or any security party hereunder or under any of the security documents after the same shall have become due by the borrower or any security party.

Is the guarantee 'a mere guarantee' or an 'on demand guarantee'?

I In constructing a contract of guarantee (as with other contracts), one should start by looking at the instrument as a whole in order to see what the parties had in contemplation at the time when the contract was made (*United*

Merchant Finance Bhd v Hockwood Holdings Sdn Bhd & Ors [1999] 5 MLJ 85 at pp 91I and 92D–G) to determine the scope and object of the guarantee (*Bank of Scotland v Wright* [1990] BCC 663 at p 675).

Thus, in the English Court of Appeal case of *Easal (Commodities) Ltd v Oriental Credit Ltd; Banque Du Caire SA v Wells Fargo Bank NA* [1985] 2 Lloyd's Rep 546, a guarantee couched in the clause:

> We undertake to pay the said amount on your written demand in the event that the supplier fails to execute the contract in perfect performance …

was held by Ackner LJ to be payable on demand. The submission of Mr Tughendhat, counsel for the issuer of the bond, that the issuer would only be liable only if there was a breach of the underlying contract of sale by the seller was rejected.

The ruling of Ackner LJ in that case was persuasive and this was what he said:

> … if he (Mr Tughendhat) is right, the bank, by entering into the performance bond is taking upon itself the obligation of deciding the merits of a dispute of a contract of sale, a function for which it is virtually common ground the bank is wholly unfitted and which the parties could not have sensibly intended … if the performance of the bond was so conditional, then unless there was clear evidence that the seller admitted that he was in breach of the contract of sale, payment could never safely be made by the bank except on a judgment of a competent court of jurisdiction and this result would be wholly inconsistent with the entire object of the transaction, namely to enable the beneficiary (of the performance bond) to obtain prompt and certain payment. There is no need to cite at any length, the well-known case of *Edward Owen Engineering Ltd v Barclays Bank International Ltd* [1978] 1 Lloyd's Rep 166; [1978] 1 QB 159 as to the general nature of a performance bond, where it is stressed that a bank is not concerned in the least between the supplier and the customer nor with the question whether the supplier has performed his obligation or not, nor with the question whether the supplier was in default or not, the only exception being where there is clear evidence both of fraud and of the bank's knowledge of that fraud.

The same construction was applied in our own jurisdiction in the Federal Court case of *Government of Malaysia v South East Asia Insurance Bhd* [2000] 3 MLJ 625, where the performance bond issued by the insurance company in that case had read at p 631F:

> The guarantor shall pay damages to the Government a sum not exceeding RM420,645 within three months *upon a receipt of a written notice demanding that the guarantor pays the Government for any breach of the contract's obligations under the contract*, … (Emphasis added.)

Mohamed Dzaiddin FCJ (as he then was), following Ackner LJ in *Easal* held at p 636B that:

> In our judgment, on its true construction this Gerenti Pelaksanaan is an *unconditional bond* or an *on demand bond* and all that is required to activate it is a written demand (*Easal*). It is simply a performance bond whereby the insurance company guarantees performance by the Contractor of the works under the said contract, and in the event of non performance or any breach of

A the terms thereof, the insurance company undertakes to pay the Government a sum not exceeding RM420,645 upon a formal demand. (Emphasis added.)

In fact, in the earlier case of *China Airlines Ltd v Maltran Air Corp Sdn Bhd* [1996] 2 MLJ 517 at p 534B, the Federal Court had found it necessary to define and distinguish between a conditional and an unconditional B performance bond in the following passage of the judgment of the same judge:

> A bank guarantee is a performance bond. There are two types of performance bond. The first type is a conditional bond whereby the guarantor becomes liable upon proof of a breach of the terms of the principal contract by the principal and the beneficiary sustaining loss as a result of such breach. The C guarantor's liability will therefore arise as a result of the principal's default. The second type is an unconditional or 'on demand' performance bond which is so drafted that the guarantor will become liable merely when demand is made upon him by the beneficiary with no necessity for the beneficiary to prove any default by the principal in the performance of the principal contract.

D It is clear that the guarantee that the parties had entered into was a performance bond, or properly so called, a performance guarantee, struck with the intention of protecting the bank against the non-payment of the money loaned to the borrower under the facility agreement. The terms and conditions written therein must therefore be given the precise construction that the contracting parties had intended. As Peh Swee Chin FCJ said in *Esso* E *Petroleum Malaysia Inc v Kago Petroleum Sdn Bhd* [1995] 1 MLJ 149 at p 156:

> That the real issue of a performance bond is one of contractual interpretation … it involves a straightforward exercise of construction, or interpretation, of the bond to discover the intention of the parties — per Sir Denys Buckley in *IE Contractors* [1990] 2 Lloyd's Rep 496 at p 503; (1991) 51 BLR 1 at p 15.

F Looking at the guarantee as a whole, it would be totally inconceivable under the circumstances to expect that the parties had intended the guarantee to be operative only if the bank is free from any cross-claims from the borrower as counsel for the defendants submitted. Such a construction would be wholly inconsistent with the purpose of providing the required security or protection to the bank that the parties had intended.

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It would of course be perfectly open to the guarantors to provide a conditional guarantee — to make the guarantors liable to pay the bank only if the borrower did not have any cross-claims against the bank, but this would have to be stated in clear terms in the guarantee. As it was, the guarantors in the instant case had given the bank an unconditional H guarantee that they would pay the bank on demand upon the happening of the 'event of default' which the borrower had failed therefrom to remedy.

The guarantee that the defendants had given to the bank was clearly a demand guarantee. All that was required to activate the guarantors' liability to pay in this case was the default of the borrowers to which a demand had I been made to the guarantors to pay.

Except to serve the subsidiary purpose of providing a 'reference point' to determine their liability to pay, the guarantors' liability on the guarantee

itself is independent of the facility agreement and any other agreements that the borrower or any third party had signed with the Bank to provide security for the loans, including the debenture and the charge which is the subject matter of the borrower's claim against the Bank in the other suit referred to in the submission.

The fact that the borrower may have a claim against the bank in respect of its failure to comply with its promise to release the unused portion of the land secured under the debenture and the charge as provided under cl 11 of the facility agreement would not therefore discharge the guarantors from their obligation to pay.

A question of co-extensiveness

At first blush, the construction may appear to conflict with the established principle that a guarantor's obligation in a contract of guarantee (as opposed to a contract of indemnity) is coextensive with the liability of the principal contractor.

The principle may be better understood by referring to the following passages in paras 44–051 and 44–066 of *Chitty on Contracts* (Vol 2) *Specific Contracts* which read:

> In contracts of guarantee, there is a prima facie rule of construction that the surety's obligations are coextensive with those of the principle debtor… Many consequences flow from the principle of coextensiveness; in particular many of the rules relating to the discharge of the surety are often treated as dependent on the principle. … If the debtor is discharged not so much because the agreement is fully performed, but rather because, in point of law, he is not liable to the creditor under the agreement in the events which have happened, as, eg where a bailee is discharged because the goods are stolen from him without any negligence on his part, a guarantor will also be discharged.

The principle appears to form the basis of the defendants' submission that they would be discharged from their guarantee should the court find (in the other suit) that the borrower is not liable to pay the bank. That submission, with respect, has also been misconceived. The coextensiveness of the guarantor has to be determined by his obligation under the guarantee. Here, the guarantors' obligation to pay was hedged on the happening of an 'event of default' of the borrower to pay the outstanding sums of money owed to the bank on demand. The co-extensiveness in this case was the obligation of the borrower to pay on demand upon the cancellation of the loan facility by the bank and not the general liability to pay the loan to the bank as in a contract of guarantee per se.

The decision of the House of Lords in the *Trafalgar House Construction (Regions) Ltd v General Surety & Guarantee Co Ltd* [1995] 3 All ER 737 (correctly distinguished by the Federal Court in *Government of Malaysia v South East Asia Insurance Bhd*) serves to illustrate the point. There the issue before their Lordships was whether a bond which provides a guarantee that the guarantor 'shall satisfy and discharge the damages sustained by' the main contractor whom it had stood guarantee for up to an amount of the bond was liable on the said guarantee. Construing the bond in that case to

A be not an 'on demand bond', it held (per Jauncey LJ, overruling the Court of Appeal), that 'proof of damage, and not mere assertion thereof is required before liability under such a bond arises'. The coextensiveness in that case was the liability to pay only upon proof of damages sustained by the main contractor at the end of the day, quite unlike the defendants' liability in the instant case to pay 'on demand'.

B

Finding — the second issue

The submission calls for the determination of whether the failure or refusal of the bank to disclaim all its rights to the remaining portion of the land not occupied by the building pursuant to cl 11 of the facility agreement C constitutes a variation of the agreement that would discharge the guarantors from the guarantee.

Essentially, a variation of an agreement occurs when the parties to a contract mutually agree to alter its terms by oral or written agreement. The agreement which varies the term of a contract must be supported by D consideration (see paras 23–32 and 23–034 of *Chitty on Contracts* (Vol 1) *General Principles* (28th Ed).

Assuming that the Bank had not kept to its promise to provide the borrower with the requisite letters of disclaimer disclaiming all its rights to the remaining portion of the land pursuant to cl 11 of the facility agreement E despite the borrower having properly provided a valuation of RM210m, all that could have arisen from such a failure would be a breach of a term and condition of the facility agreement to which the borrower may be able to bring a cross-claim against the Bank.

The default on the part of the Bank to keep to its promise (even if proved to be a breach) cannot by any stretch of the imagination constitute F a variation of the facility agreement. I am therefore bound to conclude that counsel's submission on this issue has been totally misconceived.

But even assuming by a long shot that the failure of the Bank to release the land in breach of its obligation under cl 11 of the facility agreement can be construed as a variation of the term and condition of the agreement, the G guarantee itself has made provisions for such eventualities under cl 5 which, inter alia, provides that the guarantee shall not be affected or be released by any variation or modification in the securities given under the facility agreement.

An authority directly on point can be found in *Citibank NA v Ooi Boon* H *Leong & Ors* [1981] 1 MLJ 282 at p 284B wherein Raja Azlan Shah CJ (as he then was) in having to deliberate on a similar exclusion clause in a contract of guarantee, ruled as follows:

> Clause 16 enables the bank, at its absolute discretion and without notice to or consent of the respondents (the guarantors), to vary or alter the contract between the bank and the company (the borrower) and that any right of the I respondents which is inconsistent with the terms of the contract has been waived by them. In other words, there was a voluntary waiver of the rights of the respondents to be subrogated on payment of the loan.

With respect to s 86 of the Contracts Act 1950, this was what his Lordship said at p 283G:

> The section provides express provision for the respondents to consent to any variation. They are the sole judges whether or not they will consent to remain liable notwithstanding such variation, and that if they have not so consented they will be discharged.

By subscribing to the terms and conditions described in cl 5 of the guarantee, it is clear to me that the defendants had waived whatever right that they may have had over any variation that the Bank may have instituted over the charged property.

The decision

The plaintiff's claim clearly falls within that category of cases envisaged by Azmi SCJ in *Bank Negara Malaysia v Mohd Ismail & Ors* [1992] 1 MLJ 400 at p 408G (with respect to the duty of the court in hearing an O 14 application for summary judgment):

> Where the issue raized is solely a question of law without reference to any facts or where the facts are clear and undisputed, the court should exercise its duty under O 14. If the legal point is understood and the court is satisfied that it is unarguable, the court is not prevented from granting a summary judgment, merely because 'the question of law is at first blush of some complexity and therefore takes a little longer to understand' (see *Cow v Casey* [1949] All ER 197; and *European Asian Bank AG v Punjab & Sind Bank* [1983] 2 All ER 508 at p 516).

The 'underlying philosophy in the O 14 provision' to quote Hashim Yeop A Sani SCJ in *Malayan Insurance (M) Sdn Bhd v Asia Hotel Sdn Bhd* [1987] 2 MLJ 183 at p 185, 'is to prevent a plaintiff clearly entitled to the money from being delayed his judgment where there is no fairly arguable defence to the claim'. The O 14 procedure, so it was ruled in that case, 'should only be applied to cases where there is no reasonable doubt', or to use Thompson CJ's dictum in *Syn Lee & Co Ltd v Bank of China* [1961] MLJ 87, 'where there is a moral improbability of a very high degree that the defendant can succeed'.

That there is a very high degree of moral improbability that the defendants can succeed in this case is clear. The facts are undisputed. The issues are purely issues of law that can be resolved within the four corners of the guarantee itself; and nothing in that guarantee can possibly be construed to read in favour of the defendants that they need not have to pay on demand. In short, there is clearly no defence to the plaintiff's claim.

The appeal is dismissed with costs. There shall be an order in terms of this application.

Appeal dismissed.

Reported by Peter Ling